# Finance For Growth: Here and Now…and Next

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**Viewpoint**

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Fabrizio joined Muzinich in June 2018. Prior to that he was in the public sector where he has held a number of roles including most recently Head of the Office of Italy's Minister of Finance, responsible for developing policies targeting macroeconomics, tax, finance and banking. Before that he served as G20 Sherpa and Senior Economic Counsellor to the Italian prime minister. Previously, during his time at the OECD in Paris, he also held the role of Chief of the Sherpa Office and Special Counsellor to the Secretary General in Paris, responsible for coordinating the OECD's contributions to the G20 and G8 during and after the financial crisis. He holds a degree in International Affairs from the Scuola S. Anna in Pisa and a Masters in International and European Law from the European University Institute.

### *Evolving policy initiatives are broadening the scope for small and medium-sized enterprises to access financing*

European small and medium-sized enterprises (SMEs) have products and markets. They are able to innovate in what they produce and the way they produce. They are also strong in exporting by making inroads into new markets or penetrating deeper into existing markets; in 2017 French SMEs exported more than €470bn.[1]

Vis-à-vis these strengths however, SMEs often struggle to find financing, or to find the right financing.

Traditionally the real economy in Europe has been financed through bank credit in its various forms. This channel is becoming progressively less efficient.

Regulations and supervisors are steering banks towards more asset-light models, with a possible "negative impact on loan supply in the short-to-medium term as banks adjust their balance sheets to reduce their risk-weighted assets".[2]

We believe this trend is likely to shape the relationship between the financial sector and the European industry over the long term. Even during periods of accommodative central bank monetary policy, long-term credit funding for SMEs is not always readily available, in our opinion.

Conditions are not uniform in the eurozone and may vary greatly from country to country. However, the European Central Bank (ECB) itself, in its "Survey on the Access to Finance of enterprises in the euro area", recently reported that "particularly for bank loans, one of the most important means of funding for SMEs, the net percentage of respondents indicating improved availability declined to 9%". [3]

1. BPI, "Annual Report on SMEs 2018"
2. Financial Stability Board, "Evaluation of the effects of financial regulatory reforms on small and medium-sized enterprise (SME) financing", 7 June 2019
3. Source: ECB, October 2018 to March 2019

This is why we believe in Finance for Growth! Different funding instruments are brought together under this catchphrase, such as growth capital and private debt in its various forms, which provide funding for small to medium-sized corporations through capital markets.

In Europe, we believe this alternative means of financing has emerged and become progressively well-known over the last fifteen years. However, only recently has its availability become widespread across Europe, as the result of factors including policy actions, market trends and savings needs.

### Policy Improvements

Governments have become more attentive to the issue of SME financing and have implemented measures to facilitate financing access in key countries and at the broader European level.

Italy has introduced a set of tools to direct small businesses towards capital markets, such as legislation on mini-bonds (securities issued by SMEs), corporate governance reforms to facilitate listing, and tax breaks, such as the Piani Individuali di Risparmio (PIR), for investing in SMEs.[4]

Equally in France, the recent adoption of the Loi Pacte has introduced measures to strengthen and diversify business financing.[5]

The same objectives have been pursued at the European level through the Capital Market Union (CMU) which, among other measures, has introduced the European Long-Term Investment Fund (ELTIF), which provides a continent-wide framework to collect and channel savings to SMEs.[6]

### Increasing Support from Asset Managers

Asset managers are providing more resources. For example, in the first quarter of 2019, direct lenders in Europe originated €2.5bn, which is three times higher than in the first quarter of 2018.[7]

The type of investment products available have also increased and now include a broader range of solutions such as diversified credit funds, which can carry out parallel lending alongside banks.

### Expanding Access for Private Investors

We are also seeing the increasing trend for private savers to invest in alternative instruments. Private equity and private debt funds have traditionally been the domain for institutional investors and high-net-worth individuals.

Today, law makers and regulators are more open to allowing access for European retail investors, through instruments such as ELTIFs or fund-of-funds, to investments in illiquid instruments.

However, the attractiveness of possible long-term returns and the social impact of contributing to financing the local economy will have to be balanced with illiquidity risk and regulatory requirements.

While this is a moving framework, we believe this trend is here to stay and new instruments are likely to continue to emerge in accordance with the innovation capacity of assets managers and investors.

In our view, this makes sense in a period of ultra-low or negative interest rates, which may see yields from more traditional instruments compressed for a long time to come.

4.https://www.globalcapital.com/article/kbgmwr0wn362/italy-innovates-with-minibonds-to-fill-sme-lending-vacuum; https://www.ft.com/content/6b5461b8-0127-11e8-9650-9c0ad2d7c5b5
5. https://www.gouvernement.fr/en/pacte-the-action-plan-for-business-growth-and-transformation
6. https://october.eu/capital-markets-union-2-eltif-funds/
7. "European Direct Lending Perspectives", Issue 2 – Q1 2019 Review by Creditflux / Debtwire